Internal Revenue Service

U.I.L. No.: 1362.04-00

Department of the Treasury

Washington, DC 20224

199912037

Contact Person:

Telephone Number:

In Reference to:
CC:DOM:P&SI:3 PLR-116844-98

Date: DEC 17 1998

Legend

Company =

State =

Trust =

Husband =

Wife =

a =

b =

c =

d =

Dear

This letter responds to a letter dated August 26, 1998, and supplemental information, requesting a ruling under § 1362(f) of the Internal Revenue Code on behalf of Company.

The information submitted discloses that Company was incorporated in State on a. Company subsequently elected to be an S corporation effective on b.

Company's former shareholder, Husband, who held all of Company's stock in his grantor trust, died on c. On Husband's death, his trust became irrevocable and no longer qualified as a grantor trust.

Immediately upon Husband's death, Trust was established under the provisions of his grantor trust, and was funded with the Company stock formerly held by his trust. It is represented

that Trust qualified as a "qualified subchapter S trust" ("QSST") within the meaning of § 1361(d)(3), with Wife as its sole income beneficiary. However, due to confusion following Husband's death, Wife failed to make a QSST election under § 1362(d)(2).

On d, during the preparation of Husband's federal estate tax return, it was discovered that Company's S election had terminated on c, as a result of Wife's failure to make an election under § 1361(d)(2). After a lengthy illness of its accountant, Company and its attorney took steps to remedy this situation by submitting a request for relief under § 1362(f).

Section 1361(b)(1)(B) provides that the term "small business corporation" means a domestic corporation that is not an ineligible corporation and that does not have as a shareholder a person (other than an estate and other than a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1361(c)(2)(A)(i) provides, in part, that for purposes of § 1361(b)(1), which defines the term "small business corporation," a trust all of which is treated (under subpart E of part I of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(d)(1) provides that in the case of a QSST with respect to which the beneficiary makes an election under § 1361(d)(2), the trust shall be treated as a trust described in § 1361(c)(2)(A)(i), and for purposes of § 678(a), the beneficiary of the trust shall be treated as the owner of that portion of the trust that consists of stock in an S corporation with respect to which the QSST election is made.

Section 1361(d)(2)(D) provides that an election under § 1361(d)(2) shall be effective up to 15 days and 2 months before the date of the election.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1st day of the 1st taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or (B) was terminated under paragraph (2) or (3) of § 1362(d); (2) the Secretary determines that the circumstances resulting in the

ineffectiveness or termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents; and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary for that period, then, notwithstanding the circumstances resulting in the ineffectiveness or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Applying the relevant law to the facts submitted and the representations made, we rule that the termination of Company's subchapter S corporation election, which resulted from the failure of Trust to make a QSST election under § 1361(d)(2) as described above, was an "inadvertent termination" within the meaning of § 1362(f).

Pursuant to the provisions of § 1362(f), Company will be treated as continuing to be an S corporation from a, until the QSST election is filed, and thereafter, provided Company's election is not otherwise terminated under § 1362(d). During that period, the Trust will be treated as a trust described in § 1361(c)(2), assuming it qualifies as a QSST described in § 1361(d)(3), and Wife must be treated for purposes of § 678 as the owner of Trust. If Company, the Trust, or Wife fail to treat Company, Trust, and Wife as described above, this ruling shall be null and void.

Except as specifically set forth above, we express no opinion concerning the federal tax consequences of the foregoing facts. In particular, we express no opinion regarding whether Company otherwise qualifies as a valid S corporation, the Trust qualifies as a QSST under § 1361(d)(3), or the QSST election made for the Trust is valid.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely yours,

JEFF ERICKSON
Assistant to the Chief
Branch 3
Office of the Assistant
Chief Counsel
(Passthroughs and Special
Industries)

Enclosure (1)
Copy for § 6110 purposes